

Clear Skies: Celestial preserves operating lessors' interests

The Court in *Celestial Aviation Trading 71 Limited v Paramount Airways Private Ltd* [2010] EWHC 185 (Comm) has confirmed that a defaulting lessee under an aircraft operating lease is not entitled to relief against forfeiture. An operating lessor, which has not been paid its rent, can terminate the lease and get its aircraft back.

Celestial had leased three aircraft (with a useful life of at least twenty years) to Paramount under eight year operating leases. Paramount consistently failed to pay on time the rent and supplemental rent due to Celestial. Celestial eventually terminated the leases and sued Paramount: (a) for monies due under the leases; and (b) sought delivery up of the aircraft. Paramount sought the equitable remedy of relief from forfeiture in respect of the aircraft, on the basis that the only default leading to termination was failure to pay monies due.

Prior to the *Celestial* case, it was widely considered that relief against forfeiture would only be given in limited cases, such as where the lessee has breached its strict payment obligation for administrative reasons (eg if a payment instruction was delayed, or if the lessee was short by a couple of dollars). Conversely, the Court was thought less likely to grant relief where non-payment was due to deliberate disregard by the lessee of its obligations, or to a persistent failure to pay on time.

However, at the summary judgment hearing ([2009] EWHC 3142), Mr Justice Teare gave judgment for the unpaid rent, but surprisingly sent to trial the issue of whether the defaulting lessee was entitled to relief against forfeiture.

At trial, the Court reaffirmed that it had jurisdiction to grant relief where: (i) the contract involves the transfer of proprietary or possessory rights; (ii) the right to forfeit has been inserted in the contract essentially to secure the payment of monies; and (iii) policy supports the existence of the jurisdiction.

Whilst Mr Justice Hamblen accepted that the operating leases in this case transferred possessory rights to the lessee, he considered that it would represent a major extension of existing authority for the relief jurisdiction to apply to contracts transferring a bare possessory right for only a proportion of the economic life of a chattel, such as an aircraft.

He therefore drew a distinction between leases for "indefinite" possession of the chattels (as in *On Demand Information Plc v Michael Gerson (Finance) Plc* [2001] 1 WLR 155), which qualify the owner's property interest; such leases he equated as "analogous" to a contract where the lessee ultimately acquires ownership or where the expectation is that ownership will transfer (such as a hire-purchase contract), and the present case, where Paramount only had a right to possess the aircraft for a proportion of its economic life and the lease contained no purchase option and had detailed terms of return and redelivery of the aircraft.

Key Issues

Court's jurisdiction to grant relief from forfeiture

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He considered that Celestial, as lessor, retained a very real interest in the aircraft themselves, including their proper maintenance, the extent of their use, condition, and their rental and retail value, and therefore retained many of the risks and rewards of ownership. In addition, rent was not calculated on the basis of recouping the cost of the aircraft, together with interest and profit, but reflected Celestial's residual interest.

Mr Justice Hamblen therefore considered that this continuing interest in the aircraft themselves, and not just the payment of rent, meant that it could not be said that the essential purpose of the lease's termination provisions was as "security" for the payment of rent. Rather, the purpose of these provisions was to secure Celestial's ability to be released from the leases and to have the aircraft returned if Paramount was in default.

As to policy, Mr Justice Hamblen was not prepared to hold that clauses making time of the essence necessarily excluded the relief jurisdiction. However, he did conclude that the need for certainty in commercial contracts for valuable assets, such as aircraft, pointed strongly against the court having power to relieve against forfeiture. If the Court had jurisdiction in this area, an aircraft lessor would not know whether and, if so, when it could terminate a lease or whether it would be prevented from relying on the termination provisions of its leases. The judge concluded therefore that the Court had no jurisdiction to grant relief in relation to operating leases of this nature.

Further, even if the Court had jurisdiction, Mr Justice Hamblen would not have granted relief in this case, where significant sums were due in respect of each aircraft and Paramount had given no proper explanation as to how and why the defaults had occurred, notwithstanding the length of time the sums had been outstanding and the warnings which had been given.

Aircraft lessors can therefore be assured of their position in the case of an operating lease for a term less than the useful life of the aircraft and where the lessor retains most of the risks and rewards of ownership. In the case of finance leases however, relief may still be a possibility and industry participants should be aware of this.

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